



Assessing the impact of the Chinese stimulus package at home and abroad: A damp squib? ☆



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ABSTRACT

The November 2008 Chinese stimulus package seemed to provide almost ideal preconditions for governmental success based upon its size, its concentration on infrastructure, accompanying fiscal expansion at the local level, and supportive expansions in bank lending rates. Our sectoral-level analysis suggests that investor reactions were quite tightly focused, however, with Shanghai market outperformance concentrated primarily in the nation's property, construction, and building materials sectors. Further significant post-stimulus gains accrued to the specifically targeted automobile, steel and textile industries. Meanwhile, Chinese company listings in Hong Kong and New York evinced little sectoral outperformance.

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"We think China has it right ... The majority of their package is on infrastructure spending. We are seeing life there. We are seeing the turnaround. We would like to see a more robust infrastructure package [in the United States]."(Caterpillar Chief Financial Officer Dave Burritt, 2009)¹

"In China, we have an old saying: 'If it's medicine, it will have some poison inside' ... So the stimulus must have some bad effects."(Guo Tianyong, Central University of Finance and Economics, 2010)²

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¹ As quoted in Garza (2009).

² As quoted in Richburg (2010).

1. Introduction

The Keynesian premise that fiscal stimulus is key to bringing an economy out of recession was seemingly challenged by the rather muted response of the US economy to the deficit spending programs enacted by President Obama (cf. [Ohanian, Taylor, & Wright, 2012](#)). There were abundant grounds for believing that the Chinese stimulus program should be more effective, however. First of all, the 4 trillion renminbi stimulus program announced by the Chinese government in November 2008 (equivalent to \$586 billion at the time) represented around 15% of the country's GDP and therefore considerably exceeded the US package in relative size. Second, unlike the US case, infrastructure spending played a particularly prominent role, accounting for approximately 72% of the total package ([McKissack & Xu, 2011](#)). Indeed, the series of megaprojects launched by the Beijing government since the onset of the global financial crisis were of such scope as to likely confer significant spillover effects on Taiwan as well as the mainland Chinese economy itself ([Chen, 2011](#)). Third, the central government's investment plan was substantially augmented by local government spending initiatives. Unlike in the United States, where cutbacks by state and local governments worked to offset the aggregate fiscal spending increase, local governments in China boosted spending in support of the central government program ([Fardoust, Lin, & Luo, 2012](#)). The provincial government of Guangdong, for example, planned to invest as much as 2.37 trillion renminbi over the 2009–2013 period quite aside from the national plan ([Zhu, 2012](#)). Meanwhile, the overall funds committed to infrastructure by the central government alone exceeded total new US infrastructure funding by more than three to one, even though the US economy is itself approximately three times the size of China's.³

Besides the nature of the fiscal stimulus program itself, the Chinese spending increase occurred in an environment where the multiplier effect appears to have been consistently higher than in the United States over the post-1978 reform period. [Wang and Wen \(2013\)](#) find a multiplier effect in excess of two for both central and local government expenditures in China. Implementation of the Chinese stimulus package was further aided by soaring fixed asset investment by the central government's state-owned enterprises (SOEs). Such SOE investment jumped from an annualized growth rate of 11.59% in the second quarter of 2008 to 45.3% in the second quarter of 2009 ([Wen & Wu, 2014](#)). [Wen and Wu \(2014\)](#) also note that this was fueled by increased borrowing such that, even as private manufacturing firms lowered their leverage ratios in the face of the crisis, the SOEs raised their average leverage ratio from 57.5% in the first quarter of 2008 to a peak of 61.4% in the second quarter of 2009. This was possible because, whereas US banks largely sat on the vast amounts of liquidity generated by the Federal Reserve since 2008, the Chinese state-owned banks vigorously expanded their lending as the People's Bank of China relaxed the lending constraints that had been imposed on banks prior to the crisis. China's state-owned banks were now free to take full advantage of the guaranteed spread between lending and deposit rates afforded by the stipulated margin around the benchmark level set by the People's Bank.⁴

The actual extent and distribution of the benefits attached to the Chinese stimulus package remain open to question, however. It is widely held that substantial amounts of the funds lent were being used not in financing real economic activity but in speculation in the nation's stock and property markets.⁵ Rising bank loan issuance was accompanied by a 60% rise in the Shanghai stock market over the first six months of 2009, while the general house sale price in major cities of China increased by almost 60% from 2009 to 2011. The lending surge raised concerns about inflation and a possible bursting asset price bubble. [Zhang, Willett, and Li \(2012\)](#) note that more than half of the largest commercial banks reported over 10% growth in non-performing loans during 2010–2011 while China's credit-to-GDP ratio rose from 120% at the end of 2008 to 166% by March 2011. Concern at the pace of house price increases, especially in Shanghai, prompted the authorities to launch a series of policy initiatives targeting the housing market, which included new limits on the number of properties that individuals were allowed to own (see also [Burdekin, 2012](#)). The post-2008 house price gains in China were almost certainly fueled by the People's Bank's monetary easing and expanding bank lending—and the ongoing liquidity expansion may also have manifested itself, in part, in accompanying stock market gains. Not only should the Chinese government be concerned about home prices being pushed further and further beyond the reach of most of the population but also there may well be a significant risk of asset price inflation being channeled into aggregate price increases ([Burdekin & Tao, 2014b](#)).

Analysis of the possible aggregate effects of the Chinese stimulus package via a computable general equilibrium model suggest substantial output benefits may have been realized in this case ([Diao, Zhang, & Chen, 2012](#); [Strutt & Walmsley, 2011](#); [Zhou, Shi, Li, & Yuan, 2011](#)).⁶ Although such analysis is essentially hypothetical in nature, it is indeed the Chinese package that seemed to provide far better preconditions for governmental success than the US package based upon its relative size, its concentration on infrastructure, and supportive expansions in bank lending rates. It has been hard to quantify the actual output effects, however, not only because of the limited number of quarters since the stimulus package was enacted but also because of the concerns that are frequently voiced

³ The focus on public investment may also have provided for more lasting effects on economic growth relative to other large developing economies like Brazil and India—where both local and central government spending increases focused on more traditional recurrent expenditures ([Fardoust & Ravishankar, 2013](#)).

⁴ Subsequent to the time period covered in our empirical work, the interest rate liberalization of June 2012 made inroads into the previously guaranteed spread between lending and deposit rates—potentially reducing bank profit margins significantly ([Burdekin & Tao, 2014a](#)).

⁵ [Deng, Morck, Wu, and Yeung \(2011\)](#) argue that, whereas bank funds may initially have been lent to SOEs, these SOEs then invested the lion's share of the proceeds in real estate in search of short-term gains in a hot sector. Overbidding in land auctions by these SOEs itself may well have become a significant contributor to perpetuating and extending a bubble in China's real estate market.

⁶ The Keynesian model applied by [Whalley and Zhao \(2013\)](#) also emphasizes large automatic stabilizer effects stemming from the reduced levels of government revenues after the onset of the crisis.

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